PACIFICORP'S COMMENTS ON THE RECOMMENDATIONS FOR DESIGNING A GREENHOUSE GAS CAP-AND-TRADE SYSTEM FOR CALIFORNIA

PacifiCorp is a multi-jurisdictional, rate-regulated electric utility, providing service to customers in California, Oregon, Washington, Wyoming, Idaho and Utah. In California, PacifiCorp, doing business as Pacific Power, provides electricity to less than 50,000 customers in the upper northern portion of the state. Despite this small customer base, PacifiCorp's customers in California are likely to bear a significant burden as a result of the greenhouse gas cap and trade system adopted in the State of California.

As a preliminary matter, PacifiCorp notes that with the compressed time frame within which interested stakeholders have been allowed to submit comments on the Market Advisory Committee's recommendations, it is impossible to address each and every issue of concern relating to the proposed recommendations. Designing effective and well-reasoned elements of a cap and trade system without a clear identification of the emissions baseline and covered sectors seems premature and creates a significant potential to result in a less than optimum and inefficient program that does not account for the true program costs or impacts.

Nonetheless, PacifiCorp believes it is important to identify broad areas of concern and, as such, respectfully submits the following comments on the Recommendations for Designing a Greenhouse Gas Cap-and-Trade System for California, Recommendations of the Market Advisory Committee to the California Air Resources Board, June 1, 2007 (the "Report").

1. An Impartial Constitutional Analysis is Appropriate.

PacifiCorp strongly encourages the Committee or the California Air Resource Board to subject the plan it ultimately proposes to an objective, independent analysis by a reputable third party, external to the overseeing and implementing administrative agency, for Constitutional review. It would frustrate every purpose for a Cap-and-Trade system for it to be formulated with so much effort but delayed or ultimately overturned by a Federal lawsuit.

For example, although Decision 07-01-039 of the California Public Utilities Commission ("CPUC") and the CPUC Order Denying Rehearing dated May 24, 2007 in Rulemaking R.06-04-009 dismiss interstate commerce clause considerations raised by intervenors with respect to greenhouse gas emissions performance standards under Senate Bill 1368, the CPUC's Decision overruling commerce clause considerations in R.06-04-009 can be distinguished from the Recommendations in the Report. For example, the Order Denying Rehearing states,

> Moreover, as the Court explained in *Carbone*, the "central rationale [of the dormant Commerce Clause] is to prohibit state or municipal laws whose object is local economic protectionism…" (*Carbone*, at p. 390.) The EPS is not in this category, and therefore does not implicate the Commerce Clause.

Order Denying Rehearing of Decision D.07-01-039 at p. 4.

In contrast, the Report states at 53-54:

> the Committee believes it is appropriate to use a portion of allowance value to provide transition assistance aimed at mitigating the impact a pollution cap might have on workers or firms that are subject to strong market pressures from competitors located in un-capped jurisdictions. … We recommend that California undertake further study to determine whether any firms are likely to shut down or substantially downsize on account of competitive pressures that are directly connected to the absence of caps on global warming pollution outside of the state. We also recommend that the state evaluate whether incentives for efficiency or other clean-technology investments are sufficient to mitigate the projected economic dislocation, and if they are not, to consider direct financial assistance drawing on the allocation of allowance value.

In other words, the Committee proposes to tax out-of-state actors on imports into California, and use the money from that tax to promote the competitiveness of California enterprises against enterprises in some of those very jurisdictions. PacifiCorp makes no comment on whether this passes Constitutional muster. However, if, in the words of the Committee, "the California system is to serve as a model for the western states," Report at 48, the Committee should seek to develop a program that is Constitutional. Further, the Committee should support California Energy Commissioner Geesman's expressed position that "We are not going to do anything unconstitutional." Transcript, Docket Nos. 02-REN-1038 and 03-RPS-1078, Cal. Energy Comm., Jan. 10, 2007, p. 54 line 6.

Therefore, in addition to the commerce clause analysis, PacifiCorp brings the issue of Federal pre-emption respecting regulation of the interstate transmission system to the attention of the Committee as appropriate to be included in an independent Constitutional review. Others will no doubt occur to the Committee.

2. An Accurate Economic Analysis of a "First Sale" System is Appropriate.

It is not apparent from the Report that the Committee has considered the full economic costs of a "first sale" system. The Committee should consider certain key costs that California ratepayers and California in general will incur in a first sale program.

a. Loss of Market Liquidity.

Electricity costs will be increased not only by compliance costs, but also on account of loss of market liquidity. For at least some potential sellers to California, which could be quantified through a survey or other objective means, the opportunity cost of sales into California will be outweighed by the perceived cost of compliance with California regulation, leading sellers to leave the California market for others. The remaining participants will add an arbitrage cost that will be passed on to California, to the energy they acquire from the absent seller. An attempt should be made to quantify and present these particular costs.

Additionally, even for those selling to California, in addition to the increased costs from arbitrage and compliance, there are administrative costs, every penny of which will be passed on to California buyers, that sellers to California will incur and replicate at each seller, and at potentially higher expense for Sellers who are, in the words of the Committee, in "states where LSEs have little experience delivering energy efficiency ... ." Report at 48. These costs should be quantified as well.

b. Environmental Economics.

The "Guiding Design Principles Affirmed by the Market Advisory Committee" provide as Principle 3:

> Minimize administrative burdens and maximize total benefits to California, including … advancing other economic, environmental, and public health objectives.

Report at p. 11.

Although the Report states "Economic efficiency requires that electricity be priced at its marginal social cost", Report at 44, the social costs of induced scarcity of electricity should also be considered.

California only last summer suffered through a horrific heat event, with the energy to which it had access and its distribution and delivery infrastructure strained right up against their very limits for nearly full two weeks. Limiting imports by increasing costs and compliance burdens before suitable alternatives are available reduces the aggregate energy available to California at a critical time. Before any Cap-and-Trade program is implemented, the economic and social costs of restrictions to energy should be quantified and included. Particularly under a "first sale" approach, some generators that would otherwise be inclined to sell excess energy into the California market are likely to simply turn away from the California market sales opportunity due to the administrative and compliance burdens that would be places on them through the cap and trade program, despite the potential to recover the costs in their sales. Many Western states are experiencing significant electricity demand growth; many generators may be faced with the prospect of having to bid into an allowance market (where price is unknown) and deal with compliance complexities or the alternative of selling its excess power at a specified price under contract with greater certainty and no strings attached—a choice that may not be difficult to make for the generator, but one that will be at the expense of California electricity consumers.

3. The Unique Circumstances of Multi-Jurisdictional Utilities Must be Taken Into Account Within Any Final Rules.

It is not apparent from the Report that the Committee has considered the full economic costs of a "first sale" system on multi-jurisdictional utilities. PacifiCorp operates as a multi-jurisdictional utility known as Pacific Power in Northern California. As a multi-jurisdictional utility, the costs and wholesale revenues associated with PacifiCorp's megawatt-hour purchases, utility-owned generation and transmission and distribution system are assigned to or allocated

among six western state jurisdictions (California, Idaho, Oregon, Utah, Washington and Wyoming) for purposes of establishing retail rates.

a. PacifiCorp's Retail Sales within California is Small Compared to Overall System Retail Sales.

PacifiCorp has few customers in California (who consume less than two percent of overall retail sales by PacifiCorp). The company's Inter-Jurisdictional Cost Allocation Protocol recognizes each state's right to establish fair, just, and reasonable rates based upon the law of that state. Different states have different interests in megawatt-hour and resource procurement which may not be consistent with California's greenhouse gas policies. The design of a cap-and-trade system for multi-jurisdictional utilities should recognize and respect the authority of other state jurisdictions to approve megawatt-hour and resource purchases.

To the extent that megawatt-hour or resource purchases are approved by other jurisdictions and the output does not include allowance allocations necessary for the delivery of power into California, the rules applicable to multi-jurisdictional utilities should include a process that grants PacifiCorp an appropriate share of allowances from the overall cap and based upon California's share of PacifiCorp's total system retail sales. Doing so would ensure customers in other states do not bear the cost of California's policies. Imposition of a California policy that is likely to result in higher costs to the 98 percent of PacifiCorp's non-California customers without providing the ability of the states representing those customers to have input on the costs imposed may violate both law and public policy.

To the extent the other states in which PacifiCorp operates promulgate rules consistent with California's approach[1], the risk to PacifiCorp and its non-California retail customers will diminish. However, until such time, California should adopt an interim compliance process for multi-jurisdictional utilities.

b. Contract Shuffling.

The Committee should consider certain key costs that all ratepayers of multi-jurisdictional utilities will incur in a first sale program. PacifiCorp currently owns or has an ownership interest in approximately 7815 megawatts of nameplate capacity from coal and natural gas units located within seven western states (Arizona, Colorado, Montana, Oregon, Utah, Washington, and Wyoming). PacifiCorp does not currently own or operate any greenhouse gas producing, thermal generation within the state of California.

In 2005, PacifiCorp purchased electricity from approximately 170 different parties, using a variety of generation types, and located throughout the western United States. All of the megawatt-hours are delivered into PacifiCorp's multi-state transmission system, and treated as

[1] Within the auspices of the Western Climate Initiative, the states that have joined and are also ones where PacifiCorp has utility operations or generation assets include: Arizona, California, Oregon, Utah, and Washington. We also understand Colorado and Wyoming plan to participate in the Initiative's deliberations, but at this time as interested observers only.

system power. Again, costs are allocated to retail customers according to the Inter-Jurisdictional Cost Allocation Protocol discussed previously.

PacifiCorp believes in order to optimize its existing multi-state generation portfolio to ensure compliance with the California cap-and-trade program, while minimizing costs impacts to its retail customers, it may be appropriate for PacifiCorp to revise its Inter-Jurisdictional Cost Allocation Protocol, or possibly even abandon it, in order to reassign what are currently shared, system resources, both megawatt-hour purchases and generation output from utility-owned assets, in order to meet California compliance obligations.

On the subject of reassigning existing resources, the Report states at 41:

> A potential difficulty associated with imported power is "contract shuffling." The introduction of a California cap-and-trade program could induce wholesalers of out-of-state power to shift the assignment of existing sources so that sources with relatively lower emissions are assigned to California load while relatively dirtier sources meet demand elsewhere. This shuffling of contracts could reduce the emissions attributed to California imports, even though no actual reduction in emissions had taken place.

Although not technically a wholesaler of out-of-state power into California within this context, PacifiCorp's reassignment of the output from its system resources is likely to be construed by some parties as "contract shuffling". Nonetheless, we believe it is an appropriate and reasonable response by PacifiCorp, as a California regulated investor-owned utility in order to optimize the use and value of our existing multi-state generation portfolio.

In sum, PacifiCorp believes California should develop a greenhouse gas cap-and-trade system with an interim compliance process for multi-jurisdictional utilities, that takes into account their unique circumstances and existing practices, until such time a broader regional or national greenhouse gas cap-and-trade program is in effect.

4. General Comments.

Another note for consideration – the "first seller" cap-and-trade approach seems to contemplate that all of the electricity generation sources will be included within the cap and, presumably obligated to participate in mandatory reporting. We question whether it is appropriate to impose such a burden for most renewables, when most of these sources will not emit any direct greenhouse gas emissions.

Finally, PacifiCorp strongly encourages the Committee or the California Air Resources Board to analyze the impact the cap-and-trade market may have on the existing Renewable Portfolio Standard program and the greenhouse gas emissions performance standard.

Respectfully submitted this 15th day of June, 2007,

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